IN THE

Supreme Court of the United States

October Term, 1978

No. 78-[illegible]

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

v.

AMERADA HESS CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF FOR RESPONDENT AMERADA HESS CORPORATION IN OPPOSITION

NORMAN SIMMON
425 Park Avenue
New York, New York 10022
Counsel for Respondent
Amerada Hess Corporation

Of Counsel:
KAYE, SCHOLER, FIERMAN,
HAYS & HANDLER

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IN THE

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October Term, 1975

No. 75-558

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

v.

AMERADA HESS CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF FOR RESPONDENT AMERADA HESS CORPORATION IN OPPOSITION

Opinions Below

The findings of fact and opinion of the Tax Court (Pet. App. 37a-81a)[1] are officially reported at 61 T.C. 189. The opinion of the Court of Appeals (Pet. App. 1a-36a) is reported at 517 F.2d 75.

[1] "Pet." references are to the petition in White Farm Company v. Commissioner, No. 75-375. "Pet. App." references are to the separately bound appendix to the petition in No. 75-375.

Jurisdiction

Petitioner invokes this Court's jurisdiction under 28 U.S.C. §1254(1). The judgment of the Court of Appeals was entered on May 13, 1975. Rehearing and Rehearing en banc were denied on June 19, 1975 (Pet. App. 82a-83a).

Statute and Regulation Involved

Section 1001(b) of the Internal Revenue Code of 1954 (26 U.S.C.§1001(b)) provides in relevant part:

> "The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. * * *"

Treasury Regulation (26 C.F.R.) Section 20.2031-2(b)(1) provides in relevant part:

> "* * * [I]f there is a market for stocks or bonds, on a stock exchange, in an over-the-counter market, or otherwise, the mean between the highest and lowest quoted selling prices on the valuation date is the fair market value per share or bond."

Question Presented

Whether the Court of Appeals was correct in concluding that the fair market value of listed stock, under section 1001(b) of the Internal Revenue Code of 1954 (26 U.S.C. §1001(b)), should be determined by the mean stock exchange price on the valuation date, less an adjustment to account for the large number of shares involved.

Statement of Case

In this case and its companion case,[2] the Court of Appeals reversed decisions of the Tax Court and held in accordance with the position urged by the Commissioner of Internal Revenue and respondent herein Amerada Hess Corporation ("Hess").

White Farm Equipment Company ("White Farm"), whose position was rejected by the Third Circuit, has filed a petition for a writ of certiorari (No. 75-375) in the companion case. The Solicitor General, on behalf of the Commissioner of Internal Revenue, is opposing the grant of certiorari in that case. However, in order to insure that the valuation of the shares in issue will be treated consistently by both parties to the transaction, the Commissioner has filed a protective petition in this case seeking review only in the event that this Court grants the petition of White Farm.[3]

Respondent Hess is the successor in interest to Oliver Corporation ("Oliver") which sold its farm equipment manufacturing business to White Motor Company ("White Motor") on October 31, 1960. Upon this sale, Oliver received 655,000 shares of White Motor stock, cash in the amount of $1,508,550 and White Motor assumed $281,396 of Oliver's liabilities (Pet. App. 12a). White Farm, peti-

[2] White Farm Equipment Co. v. Commissioner, which was consolidated with this case before the Tax Court and the Court of Appeals.

[3] Since the Commissioner and Hess are in accord in opposing the petition for review filed by White Farm in No. 75-375, this brief will respond to that petition.

tioner in the companion case, is a subsidiary of White Motor which holds the assets received from Oliver.

The Court of Appeals held that the fair market value of the shares of White Motor stock received by Oliver should be based on the mean stock exchange price on October 31, 1960, less an adjustment to account for the large number of shares involved (a so-called "blockage discount"). There is no dispute that October 31, 1960, the date of the sale, is the correct valuation date to be used in determining the fair market value for federal income tax purposes of the White Motor shares received by Oliver (Pet. App. 16a, n.29). The mean stock exchange price of White Motor stock on the New York Stock Exchange on the valuation date was $36.3125 per share (Pet. App. 12a). This price was adjusted downward to $30.85 based on the testimony of four expert witnesses presented by the Commissioner and Hess (Pet. App. 30a). No contrary testimony was offered (Pet. App. 30a, n.46).[4]

On June 23, 1960, during the negotiation of the transaction, the parties tentatively agreed on a formula for determining the relative amount of stock and cash to be received by Oliver. For this purpose, the parties assigned a formula price to the Oliver assets and a formula price to the White Motor stock (Pet. App. 4a-9a). The formula price for the White Motor stock ($48.50) was the closing stock exchange price of White Motor stock on June 23, 1960 (Pet. App. 4a). That figure, which was reflected in the

[4] Despite the absence of contradictory testimony, Judge Hunter dissented from that portion of the Court of Appeals' holding which related to the amount of the blockage discount. This dissent was based in part on Judge Hunter's belief that the Tax Court should determine the amount of the blockage discount.

agreement for the limited purpose of establishing the terms of payment for Oliver's assets (Pet. App. 27a), was found not to have been considered by the parties to have any tax or accounting significance (Pet. App. 9a).

An agreement containing this formula and setting forth the terms of the transaction was executed on October 3, 1960 between White Motor and Oliver, subject to the approval by the shareholders of both corporations (Pet. App. 5a-6a). This agreement also contained limitations upon the disposition and voting rights of the stock to be received by Oliver. These limitations were included to prevent Oliver or any other person to whom the stock was transferred from obtaining working control of White Motor (Pet. App. 10a-12a; 12a, n.19; 26a, n.41).

ARGUMENT

The Court of Appeals' decision follows a long-standing rule uniformly applied by this and other Courts, and thus presents no important question for review.

The Court of Appeals in this case held that, under section 1001(b) of the Internal Revenue Code of 1954 (26 U.S.C. §1001(b)), the fair market value of the White Motor stock received by Oliver is based on its mean stock exchange price on the valuation date, less an adjustment for blockage. The Court of Appeals thus applied a standard for the valuation of listed stock that has been consistently followed in an unbroken line of precedents: *United States* v. *Cartwright*, 411 U.S. 546, 551 (1973); *Hazeltine Corporation* v. *Commissioner*, 89 F.2d 513, 519 (3rd Cir. 1937); *W. T. Grant Co.*

v. *Duggan*, 94 F.2d 859, 861 (2d Cir. 1938); *Rogers* v. *Helvering*, 107 F.2d 394, 396 (2d Cir. 1939); *Andrews* v. *Commissioner*, 135 F.2d 314, 318 (2d Cir.), *cert. denied*, 320 U.S. 748 (1943); *Richardson* v. *Commissioner*, 151 F.2d 102, 103 (2d Cir. 1945), *cert. denied*, 326 U.S. 796 (1946); *Southern Natural Gas Co.* v. *United States*, 412 F.2d 1222, 1252 (Ct. Cl. 1969); *Bankers Trust Company* v. *United States*, 518 F.2d 1210, 1219 (Ct. Cl. 1975); *Richard E. Wiles, Jr.*, 60 T.C. 56, 63 (1973) (en banc) *acquiesced in*, 1973-2 Cum. Bull. 4, *aff'd on another issue*, 499 F.2d 255 (10th Cir. 1974).

In *Cartwright*, this Court recently stated:

> "The willing buyer-willing seller test of fair market value is nearly as old as the federal *income*, estate, and gift taxes themselves, and is not challenged here. Under this test, it is clear that if the decedent had owned *ordinary corporate stock listed on an exchange* its 'value' for estate tax purposes would be the price the estate could have obtained if it had sold the stock on the valuation date, that price being, under Treas. Reg. §20.2031-2(b), *the mean between the highest and lowest quoted selling prices on that day.*" (emphasis added) (411 U.S. at 551).[5]

All of the above cited cases recognize that, in determining the fair market value of a listed stock, the "market" is

[5] The Supreme Court in *Cartwright* adopted the position, as having "the clear ring of common sense," that mutual fund shares be given similar treatment to common stock (411 U.S. at 551). Accordingly, the Court ruled that the fair market value of the mutual fund shares should be measured by the redemption price on the valuation date, the only price that could be obtained if the shares had been sold on that date. The Court emphasized that the value of mutual fund shares, which are regularly quoted, could "easily be determined by turning to the financial pages of a newspaper." (*Id.* at 556). The same is true of determining the value of listed common stock, as in the instant case, from the New York Stock Exchange price.

the stock exchange since it provides the most objective standard of what willing buyers will pay willing sellers. Thus it has long been recognized that market means "open market" where there is one available and, in the case of listed stock, the stock exchange fulfills this criterion. *E.g., Hazeltine,* 89 F.2d at 519.

White Farm asserts in its petition that the Court of Appeals' decision in this case conflicts with decisions of this Court and other circuits (Pet. 7-14). Significantly, though, no support for this proposition is found in any of the cases cited by White Farm.

Four cases relied on by White Farm (*United States* v. *Cartwright,* 411 U.S. 546, 551 (1973); *Elmhurst Cemetery Co.* v. *Commissioner,* 300 U.S. 37, 39 (1937); *In re Estate of Williams,* 256 F.2d 217, 218 (9th Cir. 1958); *Estate of Cora R. Fitts* v. *Commissioner,* 237 F.2d 729, 731 (8th Cir. 1956)) are cited merely as standing for the "willing buyer-willing seller" definition of fair market value, as to which there is no disagreement (Pet. 11).

In *Seas Shipping Co.* v. *Commissioner,* 371 F.2d 528 (2d Cir.), *cert. denied,* 387 U.S. 943 (1967), which White Farm urges is inconsistent with the decision below (Pet. 7-10), the Second Circuit held that under the factual circumstances peculiar to that case, the Tax Court did not err in determining the value of stock received by reference to the value of certain ships sold in exchange therefor. Indeed, the Second Circuit cautioned that the method of valuation used by the Tax Court in that case "should be used sparingly and with considerable caution" (371 F.2d at 532).

The Second Circuit also said:

> "[I]t is a means which should be used only under certain limited conditions. * * * There are obvious dangers in evaluating the consideration involved in one side of a barter by determining the worth of the consideration on the other side. In the first place, the two sides of the barter may, for various reasons, not be equal in value. Secondly, the barter-equation method is in the nature of a bootstrap operation since there is usually no logical reason to start with one side rather than the other." (*Id.* at 529-30).

And, of high importance, the Court of Appeals added:

> "*The Tax Court might have valued the Mooremac stock first by looking to its trading price on the New York Stock Exchange* and then used that figure to compute the fair market value of the ten ships. Thirdly, the evidence on the value of one side of a barter may be no more reliable than that on the value of the other side." (emphasis added) (*Id.* at 530).

The Second Circuit thus explicitly recognized that in valuing stock, "its trading price on the New York Stock Exchange" is the measure the court would have approved in that case and plainly would have been applicable absent the "limited conditions" there.

As the Third Circuit recognized in the instant case, the "limited conditions" in *Seas Shipping* are clearly distinguishable from those before it in numerous respects (Pet. App. 23a, n.39). In the first place, the Second Circuit in *Seas Shipping* held that "[t]he testimony concerning the value of the ships was ample and convincing." (371 F.2d at 532). In contrast, with regard to the sale of Oliver's going farm equipment manufacturing business, the Third Circuit explicitly found that "the testimony as to asset value in

this case cannot be characterized as either ample or convincing, as it was in *Seas Shipping*. See note 44, *infra* [Pet. App. 28a]." (Pet. App. 23a, n.39).

In the second place, in *Seas Shipping* the value of the stock reflected Seas Shipping's guaranteed participation in working control of Moore-McCormack Lines by virtue of (1) the absence of limitations on Seas Shipping's right to vote its stock; (2) Seas' right to elect two directors for at least five years; and (3) employment contracts for certain of Seas' key personnel (Pet. App. 23a, n.39; 371 F.2d at 530). In contrast, White Motor negated any control possibilities by imposing limitations upon the disposition and voting rights of the stock valued in this case (Pet. App. 10a-12a; 12a, n.19; 26a, n.41); and Oliver received no extra control or voting rights. For this and other reasons noted by the court below, the Third Circuit concluded that the "limited conditions" of *Seas Shipping* distinguish it from the instant case (Pet. App. 23a, n.39).

White Farm also relies on the recent decision of the Court of Claims in *Bankers Trust Company* v. *United States*, 518 F.2d 1210 (Ct. Cl. 1975) (Pet. 11 12). The Court of Claims itself, however, expressly confirmed that the result in the present case accords with its own decision and "supports [its] reasoning":

> "The Third Circuit decision in *White Farm* [Amerada Hess v. Commissioner], which *reaches a result similar to that which we reach*, issued subsequent to the preparation of this opinion. While *that decision supports our reasoning*, we have reached our conclusion independently." (emphasis added) (*Id.* at 1217, n.5).

All of the remaining cases cited by White Farm—which are decisions of the Tax Court—are easily distinguishable

(Pet. 11).[6] More importantly, none of them rejected the stock market price as the basis on which the fair market value of an actively traded stock on an exchange is to be determined. Indeed, the Tax Court itself has endorsed the stock exchange standard. *E.g., Luther Bonham*, 33 B.T.A. 1100, 1105 (1936), *aff'd on other issues*, 89 F.2d 725 (8th Cir. 1937); *Leon R. Meyer*, 46 T.C. 65, 106 (1966), *aff'd on this issue*, 383 F.2d 883 (8th Cir. 1967); *Richard E. Wiles, Jr.*, 60 T.C. 56, 63 (1973) (en banc), *acquiesced in*, 1973-2 Cum. Bull. 4, *aff'd on another issue*, 499 F.2d 255 (10th Cir. 1974).

Finally, White Farm argues that the Third Circuit erred in holding that the mean stock exchange price of White Motor stock should be reduced by a blockage discount. The Tax Court did not reach the question because it failed to use the mean stock exchange price on the valuation date as a point of departure. The Court of Appeals, which began with the stock exchange price, then recognized that it is widely accepted that the sale of a large number of shares has a price-depressing effect (Pet. App. 18a, n.33). The Court of Appeals further noted that the record contained the testimony of four experts presented by the Commis-

[6] Three cases deal with situations equivalent to a cash purchase of the stock to be valued (Hugh M. Matheson, 31 B.T.A. 493 (1934), *aff'd*, 82 F.2d 380 (5th Cir. 1936); Aleda N. Hall, 9 T.C. 53 (1947), *acquiesced in*, 1947-2 Cum. Bull. 2; Paul A. Johnson, 39 T.C. 473 (1962), *acquiesced in*, 1963-2 Cum. Bull. 4); one case deals with the value of inchoate marital rights (Estate of Gordon A. Stouffer, 30 T.C. 1244 (1958), *rev'd on other grounds sub nom.*, Commissioner v. Marshman, 279 F.2d 27 (6th Cir.), *cert. denied*, 364 U.S. 918 (1960), *reversal disapproved*, United States v. Davis, 370 U.S. 65 (1962)); and a memorandum decision, which in any event is not regarded as a proper authority (Pet. App. 19a, n.35), involves shares constituting the major portion of the controlling block of stock in the corporation (Estate of W. E. Telling, T.C. Memo. 1944-222, 3 T.C.M. 652).

sioner and Hess who reached very similar conclusions as to the amount of the blockage discount (Pet. App. 30a). No contrary testimony concerning the appropriate blockage discount was offered (Pet. App. 30a, n.46). Under these circumstances, the Court of Appeals properly concluded that it was unnecessary to remand for a determination of this amount.

Conclusion

The Court of Appeals' decision in this case and the companion case of *White Farm Equipment Company* v. *Commissioner* involves the straightforward application of the well-established rule for the valuation of listed stock. In both cases, the Court of Appeals was correct in holding that the fair market value of the shares involved should be determined by the mean stock exchange price on the valuation date less an adjustment for blockage. White Farm's petition not only does not cast doubt on the result reached, but raises no important question meriting review. The Solicitor General, on behalf of the Commissioner of Internal Revenue, states that he is opposing the grant of certiorari in *White Farm* and, assuming that certiorari is denied there, does not seek certiorari in the instant case. The petitions in this case and the companion case should be denied.

Respectfully submitted,

NORMAN SINRICH
Counsel for Respondent
Amerada Hess Corporation

Of Counsel:
KAYE, SCHOLER, FIERMAN,
HAYS & HANDLER

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